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Affairs
on the Millennium Challenge Account
before the House Subcommittee on Domestic and International
Monetary Policy, Trade and Technology
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Mr. Chairman, members of the committee, I am pleased to appear before you to testify in favor of the enactment of the Millennium Challenge Account (MCA) legislation requested by the President.

Last March, President Bush described an exciting new approach to development assistance. He called for "a new compact for global development" linking "greater contributions from developed nations" to "greater responsibility from developing nations." The United States would lead by example, the President pledged, and increase core development assistance by 50 percent over the next three years - making \$5 billion more per year available by the third year. A Millennium Challenge Account would channel this new assistance only to "nations that govern justly, invest in their people, and encourage economic freedom."

Why a Millennium Challenge Account?

Mr. Chairman, this new foreign assistance initiative, the Millennium Challenge Account, brings together in a new and innovative way the lessons we have learned about development over the past 50 years.

- It affirms that economic growth is key to development and poverty reduction. It targets assistance to those countries that have adopted the governance, social and economic policies that enable growth and lasting development. It recognizes private sector growth as critical to sustaining health, education and other development gains and thus emphasizes a healthy climate for entrepreneurs, including respect for private property, limits on corruption, and a functioning financial system. The MCA increases the odds of spurring economic development with partner countries and, at the same time, encourages more countries to adopt growth-oriented policies.
- The MCA recognizes that development success is driven by a country's own efforts, policies and people. We can support and encourage sound efforts, but we cannot substitute for

genuine commitment to take the hard steps needed. The MCA thus proposes a true partnership in which the developing country with the participation of its citizens establishes its own development priorities and plans.

- The MCA demands accountability and results. Each successful country proposal will include clear development objectives and benchmarks. Meeting these benchmarks will be key to continued funding.

The MCA builds on the reality of the global economy, and the success of democratic institutions. It recognizes our responsibility and opportunity to help good leaders deliver on the expectations of their people. The MCA is optimistic, yet practical, about the potential of people in poor countries to chart a course to peace and prosperity with effective support. In that, it is all American. It rests on the greater recognition by developing countries that their policies and governance are the most critical keys to development. The MCA is not the sole answer. It is part of a broad array of Administration efforts to spur development that stretch from the Doha Development Agenda to initiatives on HIV/AIDs, famine and education. Along with these other efforts, the MCA supports our overall foreign policy, including the struggle against terrorism, by encouraging free, democratic and prosperous societies where people have a stake in the future and value partnership with the United States.

The Administration's vision of the MCA, as reflected in the legislation sent forward to the Congress on February 5, is profoundly positive. It affirms the ability of the poorest people in the poorest countries to improve their lives; it embraces human dignity by stressing mutually responsible and accountable partnership; and it upholds the key insight that thoughtful and participatory political and economic governance are fundamental to lasting progress.

Developing the MCA

This past year our challenge has been to implement the vision that the President put forward last March in Monterrey. In so doing, we have engaged in an intense, thoughtful and collegial interagency process involving the Departments of State and Treasury, the U.S. Agency for International Development, the Office of Management and Budget, and a number of other entities. We have also benefited greatly from the strong interest and suggestions of many. The public, especially the NGO and

business communities, have made important suggestions. We have kept other donor nations and potential MCA beneficiary countries apprised, as both have welcomed the MCA and been keen observers of our progress. Throughout this process, the involvement of the President has been central. President Bush has given an unprecedented level of direct and sustained commitment to the MCA and to development issues more generally.

After months of discussion and deliberation, the Administration came to a number of conclusions:

- The MCA should focus on development objectives;
- It must complement, not replace current assistance;
- To ensure we select only those countries that can best use assistance, the MCA requires the integrity of objective eligibility criteria;
- To combine all the new elements - a selective program partnership that gives developing nations themselves the lead role in guiding their development, and a program where results are integrated and measured from beginning to end - we decided that the MCA could not just be grafted onto existing assistance programs or structures; and
- We also concluded that to realize the promise of the MCA without a huge increase in bureaucracy, we will have to organize and run the MCA in a whole new way, requiring a clean, flexible and creative legislative mandate.

How the MCA Would Work

Mr. Chairman, to make this vision a reality, the Administration would create a new organization - the Millennium Challenge Corporation (MCC) - with one key goal: "to reduce poverty through promoting sustained economic growth in developing countries committed to implementing good policies." This innovative approach requires new thinking and new ways of doing business that can best be introduced through a new, high-profile entity. Establishing the MCC as a government corporation with a high level board will signal that MCA partnerships are not business as usual. What we are proposing is new ways of working with very strong partners and a laserlike focus on achieving sustainable results, engines of growth and models of success where track records and lessons learned are clear to see. MCA

partnerships will be based on a high standard of mutual responsibility at the upper reaches of both governments. The MCC will use the most modern and effective approaches possible. It will combine an unprecedented level of country selection rigor and accountability for results and effectiveness, with a high degree of operational flexibility. We also expect that the Board and the MCC CEO and staff will want to consult closely with Congress on the progress and activities under this innovative new initiative.

The MCC will build on development lessons-learned. It will also draw in outside expertise and oversight on an ongoing basis, tailored to the issues, countries and sectors of practical concern. We expect US development expertise, including the experience of the US profit and non-profit sectors in establishing transparent, financially accountable, effective activities, will be engaged through the MCA. We expect as well to see local for-profit and non-profit entities working side by side with the governments and other US participants. The MCC is will support developmentally sound country proposals and work carefully with MCA partners to identify those most likely to implement effectively and to build capacity within MCA countries.

A Chief Executive Officer appointed by the President and confirmed by the Senate would run the MCC. A cabinet-level board, chaired by the Secretary of State, would provide policy guidance and oversee operations. The Secretary of State, as Chairman of the Board, will exercise strong supervision of the CEO of the MCC and ensure coordination of assistance and foreign policy consistency. The Secretary of the Treasury would ensure consistency with our multilateral assistance and our foreign economic policies. The Director of OMB, as a member of the Board, would help the Board implement the President's Management Agenda priorities of improving transparency, performance and accountability in the new Corporation.

To be most effective in promoting development, the MCC will need flexible authorities with regard to personnel, funding, procurement and contracting. The Millennium Challenge Corporation will draw its staff from the best and brightest in the public, private and non-profit sectors. We envision a relatively small staff, which would serve for time-limited terms. The staff would rely heavily on contracted services for monitoring, evaluation and many services. The MCA will need the ability to contract for goods and services with the private sector, with government agencies, and with international

organizations and should be able to procure globally. To be able to respond to individual MCA country proposals, the MCA should not be restricted to specific areas of funding.

Selection: The MCA process begins with selection of qualifying countries. The eligible pool of poor countries would expand each of the first three years as MCA funding ramps up. Only the 74 countries eligible to borrow from the IDA with a per capita income below \$1,435 would be considered the first year. In FY 2005 the pool would extend to all countries with incomes below \$1,435, adding approximately 14 countries. From FY 2006, all countries with per capita income below \$2,975 (low middle income countries) would be included, adding another 30 or so countries. The per capita income ceilings and country measures are taken from the World Bank and would be adjusted annually. Countries ineligible to receive aid under the Foreign Assistance Act would also be ineligible for the MCA.

Once a year the MCA would run a competition among the eligible countries to determine which qualify for the MCA. Qualification is based on 16 indicators measuring country performance in the three areas of ruling justly, investing in people and encouraging economic freedom. Countries that do better than the median on half the indicators in each of the three categories and on the corruption indicator would nominally qualify. Because scores relate to income, countries below \$1,435 and those between \$1,435 and \$2,975 would compete separately in the indicators and selection process. Countries that qualify in the first year will not lose eligibility simply because of median changes caused by the expansion of the pool in subsequent years.

To ensure that each qualifying country is a committed development partner that meets the President's three core criteria, the MCA Board would review the results of the indicators portion of the selection process. In exercising this responsibility, the Board would take into account material information, such as trends in leadership or corruption and other recent developments. On that basis, the Board might include a country that just missed or exclude a country that "passed".

The selection process will be transparent. Transparency provides the information necessary to give poor countries incentive and direction to develop the required policies and to ensure MCA accountability. Sources for the indicators and the data for evaluating them will be posted on the MCA website.

Board decision-making will also be transparent to Congress and the public.

The indicators come from independent and analytically rigorous sources, including the multilateral development banks, academic policy institutes, international financial institutions and non-profit organizations. Data is also solicited from national sources for budget indicators to update publicly available information. The MCA will regularly review the indicators used to help select qualifying countries. Indicators may be dropped or added if it is determined doing so will help the Board of the MCC choose the most qualified countries based on the criteria of "governing justly, investing in people, and encouraging economic freedom." Any changes will be done in a way to balance the need for flexibility with the need for predictability, so that countries know well in advance by what standards they will be judged.

The MCA Contract: The implementation phase will begin after countries have been notified of their selection to the MCA. To implement the partnership between the MCC and specific MCA countries, the MCC will use time-limited, business-like contracts that set forth a commitment between the United States and the developing country to meet agreed performance benchmarks.

Developing countries will set their own priorities and identify their own greatest hurdles to development, drawing on their development strategy as reflected in their Poverty Reduction Strategy Paper or other development planning document. We will be seeking MCA country contract proposals that engage every element of an economy - government, civil society and business. The MCC will stipulate that all country contract proposals be the result of an inclusive domestic consultative process and each MCA country will identify its priority development hurdles and a program for addressing them through such an inclusive process.

The proposal should focus on a limited number of clear measurable goals critical to economic growth and development. For example, a country might decide to focus on improvements in one or two areas, such as agriculture, education, enterprise and private sector development, governance, health and trade and investment capacity building. The proposal must include objectives, a plan and timetable for achieving them, benchmarks for assessing progress and how results will be sustained at the end of the contract, delineation of the responsibilities of the

MCC and the MCA country, the role of civil society, business and other donors, and a plan for ensuring financial accountability for funds used.

The Millennium Challenge Corporation will consult with the country at every stage of the process and provide technical assistance as necessary. The MCC will review the proposal and conduct both sectoral and country evaluations, which may include government and non-government experts from outside the MCC. Selection as an MCA country alone will not guarantee automatic funding of all aspects of a country's proposed contract. The MCC may ask questions and propose modifications to the contract proposal. The MCA Board will exercise final approval of all contracts. Contract terms will be made public in both the United States and the MCA country.

The MCA contract will also be key to how the MCA is implemented in a country. The method for disbursement of funds and selection of implementing agents, for example, may be determined in the MCA contract. The MCC will disburse funds in the most efficient manner to the implementers of MCA activities. We expect our own private sector and development experts will participate and bring to bear their skills on everything from financial management and auditing, to ensuring that education programs leave no child behind.

Monitoring and evaluation to ensure accountability for results will be an integral part of every activity for which MCA funds are used. The MCC will monitor activities and systems to ensure financial responsibility and accountability for MCA assistance. It will review overall budget data to demonstrate that MCA resources and domestic and other development resources are used in a complimentary manner. It will conduct audits to ensure that data reported by recipients is accurate and complete. It will monitor achievement of specific benchmarks for measuring progress toward program goals. And, the MCC will evaluate whether MCC assistance is achieving sustainable results. The MCC will conduct monitoring and evaluation directly and through independent contractors with professional auditing expertise. All evaluations would be made public.

MCA Programs will continue to receive funding, subject to congressional appropriation, under the terms of the country's MCA contract unless they fail to meet the specific conditions for performance specified in the contract. Funding for all or part of the MCA contract could be scaled back or ended for failing to meet financial standards or to attain specific

benchmarks. On the other hand, funding could be increased if countries reach or exceed performance targets and have included "incentive clauses" in their contract. At the conclusion of the contract period, MCA assistance will end unless participant countries that have performed successfully submit a new proposal and renegotiate a new contract with the MCC.

Operations: Mr. Chairman, we know that the keys to success of any initiative as innovative as the Millennium Challenge Account lie not only in ensuring that it has a well thought out mandate and the needed authorities. It must also operate well. We have sought to give the MCA a unique identity so that it will work well with other agencies that deliver development assistance. We have kept its staff small, so that it will rely on other agencies in the field and in Washington. We have placed MCA officials in the field under Chief of Mission authority to ensure that they coordinate well with other Embassy elements, including the AID mission. And to ensure accountability, the Secretary of State, who oversees all of our foreign assistance programs, will serve as Chairman of the Board.

USAID will continue to be central to U.S. foreign assistance. The Administration is working hard to bring forward new development initiatives on agricultural development, famine, HIV/AIDS, rural poverty, trade capacity building and humanitarian relief. Under the committed leadership of Administrator Natsios, USAID will not only have a growing role in these new development assistance initiatives, but it will also be a key partner of the MCA and could implement some MCA programs. In fact, USAID programs will work in partnership with the MCA to provide technical assistance and funding for those countries that are "near qualifiers," so that they can make the policy changes necessary to qualify for the MCA. We hope that the work and resources of the MCA, which add to existing development assistance, might even help free up other development resources to make more progress in non-MCA countries.

Funding: The initial funding request for the MCA is \$1.3 billion. This is the first stage of a ramp-up that will increase to \$5 billion by 2006. That is a 50 percent increase in core US development assistance over 2001 levels, and represents an unprecedented effort to reduce poverty. We believe \$1.3 billion will provide sufficient resources for a strong start. We deliberately chose to ramp up requests over time to ensure funds would match but not exceed our ability to use them well.

What the MCA Can Achieve

Mr. Chairman, in conclusion, the Millennium Challenge Account is an innovative effort to spark international development that deserves support. While many of the elements of the MCA are not new, this will be the first attempt to integrate them into a concept that challenges countries to adopt policies that enable development, that challenges aid recipients to take the lead in a new form of partnership, and that challenges us and MCA countries alike to adopt a business-like, results-oriented approach. The MCA's goal and mission are clear: to raise countries out of poverty by promoting sustained and broadly shared economic growth. As the MCA proves itself, we expect it to influence how multilateral and other bilateral assistance programs are designed and conducted.

The Millennium Challenge Account is a key element of the overall U.S. effort to address poverty and development, which must also include existing programs of AID and others to provide humanitarian assistance and famine relief, fight HIV/AIDs, build trade capacity, and provide for economic stability and defense of key partners. We are convinced that the MCA is in our national interest. Greater prosperity in the developing world will alleviate the poverty that breeds discontent and instability. It will expand markets for American exports. It will reduce the spread of disease and pestilence. The Millennium Challenge Account will promote our own security and well-being even as it brings a better life to millions around the globe.

Mr. Chairman, members of the committee, I request your support of the "Millennium Challenge Act of 2003."